

Ndlambe Municipality

Audit Report

For the year ended 30 June 2016

Report of the auditor-general to the Eastern Cape Provincial Legislature and the council on the Ndlambe Local Municipality

Report on the financial statements

Introduction

1. I have audited the financial statements of the Ndlambe Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2016, the statement of financial performance, statement of changes in net assets, cash flow statement and the statement of comparison of budget information with actual information for the year then ended, as well as the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of Grap) and the requirements of the Municipal Finance Management Act, 2003 (Act No. 56 of 2003) and the Division of Revenue Act, 2015 (Act No. 1 of 2015) (Dora), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-general's responsibility

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with the International Standards on Auditing. Those standards require that I comply with ethical requirements, and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the municipality preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

Basis for qualified audit opinion

Irregular expenditure

6. The municipality did not have adequate systems to identify and disclose all irregular expenditure during the year, as required by section 125(2) (d) (ii) of the MFMA. The irregular expenditure disclosed in note 42 to the financial statements was understated by the R33,5 million (2015: R12,6 million) that was identified during the audit process. Due to the lack of systems, it was impracticable for me to determine the full extent of the understatement of irregular expenditure disclosed.

Qualified opinion

7. In my opinion, except for the possible effects of the matters described in the basis for qualified opinion paragraph, the financial statements present fairly, in all material respects, the financial position of the Ndlambe Local Municipality as at 30 June 2016 and its financial performance and cash flows for the year then ended, in accordance with SA Standards of Grap and the requirements of the MFMA and Dora.

Emphasis of matters

8. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Material losses/impairments

9. As disclosed in note 49 to the financial statements, material losses of R22 million were incurred as a result of water and electricity reticulation losses.
10. As disclosed in notes 4 and 5 to the financial statements, cumulative provisions for impairments of R19,4 million (2015: R22,8 million) relating to receivables from non-exchange transactions and R41,1 million (2015: R40,4 million) relating to receivables from exchange transactions were incurred as a result of irrecoverable trade debtors.
11. As disclosed in the statement of financial performance and note 31 to the financial statements, debt impairments totalling R15,1 million (2015: R16,7 million) have been expensed.

Restatements of corresponding figures

12. As disclosed in note 45 to the financial statements, the corresponding figures for 30 June 2015 have been restated as a result of errors discovered by management during 2016 in the financial statements of the municipality at, and for the year ended, 30 June 2015.

Unauthorised expenditure

13. As disclosed in note 41 to the financial statements, unauthorised expenditure to the amount of R27,7 million was incurred due to overspending of the operational and capital budget at vote level.

Additional matter

14. I draw attention to the matters below. My opinion is not modified in respect of this matter.

Unaudited disclosure notes

15. In terms of section 125(2)(e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon

Report on other legal and regulatory requirements

16. In accordance with the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report findings on the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report, compliance with legislation and internal control. The objective of my tests was to identify reportable findings as described under each subheading, but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

Predetermined objectives

17. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected development priority: Key Performance Area (KPA) 1 – Basic service delivery on pages xx to xx in the annual performance report of the municipality for the year ended 30 June 2016
18. I evaluated the usefulness of the reported performance information to determine whether it was presented in accordance with the National Treasury's annual reporting principles and whether the reported performance was consistent with the planned development priorities. I further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's Framework for Managing Programme Performance Information (FMPPI).
19. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
20. The material findings are as follows:

KPA 1: Basic service delivery

Usefulness of reported performance information

21. Section 41(c) of the Municipal Systems Act requires the integrated development plan (IDP) to form the basis for the annual report, requiring consistency of objectives, indicators and targets between the planning and reporting documents. A total of 65% of the reported targets were not consistent with those in the approved IDP or service delivery and budget implementation plan. This was due to the lack of a proper

performance management system, which led to the leadership not performing reviews, reconciliations and follow-ups.

22. The FMPPI requires performance indicators and measures to be clearly defined so that data can be collected consistently and is easy to understand and use. In addition, performance targets must be specific in clearly identifying the nature and required level of performance, and should also be measurable.

- A total of 50% of the indicators were not well defined
- A total of 27% of the indicators were not verifiable
- A total of 52% of the targets were not specific
- A total of 58% of the targets were not measurable.

23. This was because management did not consider the requirements of the FMPPI when developing the systems and processes to create technical indicator descriptions. The lack of a proper performance management system led to the leadership not performing reviews, reconciliations and follow-ups, which also contributed to this conclusion.

Reliability of reported performance information

24. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. We were unable to obtain the information and explanations we considered necessary to satisfy ourselves of the reliability of the reported performance information. The scope of our work was limited due to the absence of information systems, the auditee not being able to provide sufficient appropriate evidence in support of the reported performance information and the auditee's records not permitting the application of alternative audit procedures.

Additional matter

25. I draw attention to the following matter:

Achievement of planned targets

26. Refer to the annual performance report on pages xx to xx for information on the achievement of planned targets for the year. This information should be considered in the context of the findings on usefulness and reliability of the reported performance information in paragraphs 21 to 24 of this report.

Compliance with legislation

27. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My material findings on compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows:

Strategic planning and performance management

- 28. The municipality did not establish mechanisms to monitor and review its performance management system, as required by section 40 of the Municipal Systems Act.
- 29. Key performance indicators, including input, output and outcome indicators, in respect of each of the development priorities and objectives were not set out in the IDP, as required by section 41(1)(a) of the Municipal Systems Act and the municipal planning and performance management regulations 1 and 9(1)(a).
- 30. Measurable performance targets for the financial year were not set in the IDP for each of the key performance indicators, and with regard to each of the development priorities or objectives, as required by section 41(1)(b) of the Municipal Systems Act and the municipal planning and performance management regulation 12(1) and 12(2)(e).

Financial statements

- 31. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements identified by the auditors in the submitted financial statements were not adequately corrected, which resulted in the financial statements receiving a qualified audit opinion.
- 32. The oversight report adopted by the council on the 2014-15 annual report was not made public, as required by section 129(3) of the MFMA.

Procurement and contract management

- 33. Quotations were accepted from prospective providers who were not on the list of accredited prospective providers and did not meet the listing requirements prescribed by the SCM policy, in contravention of SCM regulations 16(b) and 17(b).
- 34. Bids were not always evaluated by bid evaluation committees composed of officials from the departments requiring the goods or services AND/OR at least one SCM practitioner of the municipality, as required by SCM regulation 28(2).
- 35. Bid adjudication committees were not always composed in accordance with SCM regulation 29(2)
- 36. Contracts were extended or modified without tabling the reasons for the proposed amendment in the municipality's council, as required by section 116(3) of the MFMA.

Expenditure management

- 37. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
- 38. Reasonable steps were not taken to prevent unauthorised, irregular, and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Consequence management

39. Unauthorised, irregular, fruitless and wasteful expenditure by the municipality was not investigated to determine if any person was liable for the expenditure, as required by section 32(2)(a)(ii) of the MFMA.
40. Authorisation of unauthorised expenditure was not done through an adjustment budget, as required by section 32(2)(a)(i) of the Municipal Financial Management Act.

Internal control

41. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with legislation. The matters reported below are limited to the significant internal control deficiencies that resulted in the findings on compliance with legislation included in this report.

Leadership

42. Leadership did not adequately oversee the implementation and monitoring of internal controls to ensure sound financial and performance management and compliance with legislation. This resulted in inaccurate, incomplete and inadequate financial and performance reporting. Leadership developed a plan to address external audit findings, but the implementation of the plan has not sufficiently addressed all the external audit findings raised in previous years.
43. Leadership has not implemented an effective performance management system that holds staff accountable and enables the leadership to instil the principle of consequence management. As a result, a large number of municipal laws and regulations were not complied with.

Financial and performance management

44. The control environment at the municipality is inadequate, with ineffective daily and monthly processing and reconciliation of transactions for performance information. The lack of a proper functioning control environment resulted in deficiencies in the record management system and underlying records. Furthermore, compliance with legislation is not monitored adequately, resulting in findings on compliance in the current year.
45. Information was at times either incomplete or did not support the financial statements and the performance report. For some areas, under both financial and performance management the regular processes of collecting, collating and reporting on credible information were not implemented, which resulted in material findings on the reported financial and performance information.

Governance

46. The implementation of the risk management strategy was not monitored. Although a risk assessment was performed, it was inadequate and not formerly adopted.

47. The internal audit and audit committee did review the adequacy, reliability and accuracy of the financial statements and performance information. However, the review on the financial statements, performance information and compliance with legislation was not adequate, as evidenced by the material misstatements identified in all three areas.

AUDITOR GENERAL

East London

30 November 2016



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence